

ST 19-03

Tax Type: Sales Tax

Tax Issue: Exemption from Tax (Charitable or Other Exempt Types)

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
SPRINGFIELD, ILLINOIS**

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS**

v.

**ABC
CORPORATION**

Taxpayer

Docket No.
Letter ID:
Claim for Exemption Number

RECOMMENDATION FOR DISPOSITION

Appearances: Robin Gill, Special Assistant Attorney General, for the Department of Revenue of the State of Illinois; JOHN DOE, *pro se*, for ABC Corporation

Synopsis:

ABC Corporation (“taxpayer”) sent a request to the Department of Revenue (“Department”) for an exemption identification number in order to purchase tangible personal property at retail free from the imposition of retailers’ occupation and use taxes. The Department denied the request, and the taxpayer timely protested the denial. An evidentiary hearing was held during which the issue presented was whether the taxpayer is organized and operated exclusively for charitable purposes under section 3-5(4) of the Use Tax Act (35 ILCS 105/3-5(4)) and section 2-5(11) of the Retailers’ Occupation Tax Act (35 ILCS 120/2-5(11)). The taxpayer is a nonprofit organization that was created to be a community organizer to improve the blighted areas of CITY, Illinois. The Department argues that the taxpayer is not organized and operated exclusively for

charitable purposes. After reviewing the record, it is recommended that this matter be resolved in favor of the Department.

FINDINGS OF FACT:

1. The taxpayer is an Illinois not-for-profit corporation that was organized on February 17, 2004. (Dept. Ex. #1, pp. 28-30)
2. According to the taxpayer's articles of incorporation, the purposes for which the corporation is organized are as follows:

Any and all exclusively charitable purposes in furtherance of the social welfare and community redevelopment of blighted areas of the City of CITY, Illinois, within the meaning of Section 501(c)(3) of the Internal Revenue Code of 1986 (or any corresponding section of any future United States Internal Revenue law) (the "Code"). (Dept. Ex. #1, p. 28)

3. The taxpayer's Organization Narrative states, in relevant part, as follows:

The Mission of the ABC Corporation is to support the development of housing and related commercial facilities that promote the social welfare of the residents of the OTHER LOCAL neighborhood, as well as, the CITY, Illinois.

We are a CITY, Illinois based 501(c)(3) organization founded in 2005. We have a 20 year plan to develop 240 units of low-income housing, new playgrounds, community gardens, a basketball court, a baseball field, a commercial strip-mall, and a community center. To date, we have built 60 units of new single family housing (we are preparing to submit a tax-credit application to build 50 units of new apartments), two community gardens, the basketball court and own an additional 70 plots of land for future development. We also provide computers for local youth and families to use for homework, job seeking, and computer literacy training. We were recently donated a 100,000 sq. ft. industrial building that we will renovate to become a Community Center this year. (Dept. Ex. #1, p. 15)

4. The taxpayer's Application for Sales Tax Exemption includes the following as the taxpayer's purpose:

To support the development of housing and social services to residents of CITY, Illinois. To date, we have built 60 new single family houses, operate two community gardens, organized a teen summer job program, and we are currently renovating a 100,000 square foot community center. (Dept. Ex. #1, p. 4)

5. LOCAL Church is located in the OTHER LOCAL neighborhood in CITY. The taxpayer's executive director does not receive a salary from the taxpayer but receives a salary from both the church and from DEF Center ("DEFC"), which is a not-for-profit that provides services to the OTHER LOCAL neighborhood such as after-school programs, summer camps, and a senior wellness program. (Dept. Ex. #1, p. 6; Tr. pp. 19-20)
6. The executive director is the only person who works for the taxpayer. The taxpayer does not have any employees who receive compensation. (Tr. pp. 19-20)
7. The church, DEFC, and the taxpayer work together to improve the community. The taxpayer was created to be the "community organizer." The taxpayer does the development work and the community planning. (Tr. pp. 8-9)
8. The taxpayer, in partnership with OTHER COMPANY, Inc., developed COMMUNITY I in 2011 and COMMUNITY II in 2015, and both COMMUNITIES are in the OTHER LOCAL neighborhood. Each COMMUNITY has 30 units of low-income housing. Low income housing tax credits were used for both developments. (Taxpayer Ex. #1; Dept. Ex. #1, p. 17; Tr. pp. 9-10)

9. COMMUNITY I and II are each an LLC, and the taxpayer is the managing general partner of the LLCs. The taxpayer receives a developer's fee for both COMMUNITY I and II. (Dept. Ex. #1, p. 21; Tr. pp. 17-19)
10. The taxpayer acquires property that it wants to either develop or keep clean for the neighborhood. Once the property is developed, ownership is transferred to another entity. (Tr. pp. 16, 25-26)
11. The taxpayer's Profit & Loss statement for the year ending December 2017 shows the following as income:

AAA PROVIDES ¹	\$XXX.00
*** Grant	XX,XXX.00
*** Bank Grant	XX,XXX.00
*** Grant	X,XXX.00
Investment Prop. Facility Rent ²	X,XXX.00
COMMUNITY II Rent	X,XXX.00
*** Care Grant	X,XXX.00
COMMUNITY I Rent	X,XXX.00
COMMUNITY II Developer Fee	XX,XXX.00
Contributed support	<u>X,XXX.XX</u>

Total Income XXX,XXX.XX (Dept. Ex. #1, p. 21)

12. The taxpayer is exempt from federal income taxes under section 501(c)(3) of the Internal Revenue Code pursuant to a determination made by the IRS. (Dept. Ex. #1, pp. 25-27)
13. The taxpayer has no capital, capital stock, or shareholders. (Dept. Ex. #1, pp. 28-30)

CONCLUSIONS OF LAW:

¹ AAA PROVIDES is a not-for-profit organization that coordinates a day when OTHER CITY residents can donate money to various not-for-profit organizations. (Tr. p. 15)

² Investment Prop. Facility Rent is rent income from a company that manages the COMMUNITY property and rents office space on the property. (Tr. pp. 15-16)

The Use Tax Act (“Act”) (35 ILCS 105/1 *et seq.*) imposes a tax upon the privilege of using in Illinois tangible personal property purchased at retail from a retailer. 35 ILCS 105/3. Section 3-5(4) of the Act provides a list of tangible personal property that is exempt from the tax, and includes the following:

Personal property purchased by a governmental body, by a corporation, society, association, foundation, or institution organized and operated exclusively for charitable, religious, or educational purposes On and after July 1, 1987, however, no entity otherwise eligible for this exemption shall make tax-free purchases unless it has an active exemption identification number issued by the Department. 35 ILCS 105/3-5(4).

Section 2-5(11) of the Retailers’ Occupation Tax Act (“ROTA”) (35 ILCS 120/1 *et seq.*) contains a similar provision for personal property sold to these organizations. See 35 ILCS 120/2-5(11). Therefore, in order to receive the exemption identification number, the taxpayer must be “organized and operated” exclusively for charitable purposes. See also 86 Ill. Admin. Code §130.2005(j)(3). The term “exclusively” is not interpreted literally to mean the entity’s sole purpose; it is construed to mean the primary purpose. Yale Club of Chicago v. Department of Revenue, 214 Ill. App. 3d 468, 473 (1st Dist. 1991); Gas Research Institute v. Department of Revenue, 154 Ill. App. 3d 430, 436 (1st Dist. 1987).

In order to determine whether the taxpayer is organized and operated exclusively for charitable purposes, the following factors are considered: (1) whether the benefits derived are for an indefinite number of people, persuading them to an educational or religious conviction, for their general welfare or in some way reducing the burdens of government; (2) whether the organization has no capital, capital stock or shareholders, earns no profits or dividends, but rather derives its funds mainly from public and private charity and holds them in trust for the objects and purposes expressed in its charter; (3)

whether the organization dispenses charity to all who need and apply for it; (4) whether the organization does not provide gain or profit in a private sense to any person connected with it; (5) whether the organization does not appear to place obstacles of any character in the way of those who need and would avail themselves of the charitable benefits it dispenses; and (6) whether the organization is actually and factually operated primarily for charitable purposes. Wyndemere Retirement Community v. Department of Revenue, 274 Ill. App. 3d 455, 459 (2nd Dist. 1995) (citing Methodist Old Peoples Home v. Korzen, 39 Ill. 2d 139, 156-57 (1968)).³ These factors are balanced with an overall focus on whether and how the organization serves the public interest and lessens the State's burden. Du Page County Board of Review v. Joint Commission on Accreditation of Healthcare Organizations, 274 Ill. App. 3d 461, 466 (2nd Dist. 1995). Whether an institution has been organized and is operating exclusively for an exempt purpose is determined from its charter, bylaws and the actual facts relating to its method of operation. *Id.*

The taxpayer has the burden of proving by clear and convincing evidence that it is entitled to the exemption. Rogy's New Generation, Inc. v. Department of Revenue, 318 Ill. App. 3d 765, 771 (1st Dist. 2000); Wyndemere, *supra*; Gas Research Institute, *supra*. It is well-settled that tax exemption provisions are strictly construed in favor of taxation. *Id.*; Heller v. Fergus Ford, Inc., 59 Ill. 2d 576, 579 (1975). All facts are construed and all doubts are resolved in favor of taxation. *Id.* To prove its case, a taxpayer must present more than its testimony denying the Department's determination. Sprague v. Johnson, 195 Ill. App. 3d 798, 804 (4th Dist. 1990); Balla v. Department of Revenue, 96 Ill. App.

³ Because these factors are also used to analyze charitable exemptions from property taxes, cases involving property taxes will also be cited. See Wyndemere, *supra*.

3d 293, 296 (1st Dist. 1981). The taxpayer must present sufficient documentary evidence to support its claim. *Id.*

The Department argues that the taxpayer is not organized and operated for charitable purposes. The Department states that the taxpayer seeks to organize community involvement and develop affordable housing. The taxpayer assembles the parties involved in the financing, construction, and management of affordable housing and receives development fees but does not own, build, or sell the properties. The Department contends that although the taxpayer is organized for noble purposes, it is not organized and operated exclusively for charitable purposes.

The Department also argues that the taxpayer does not meet the standards set forth in Methodist Old Peoples Home, *supra*. The Department acknowledges that the taxpayer does not have capital, capital stock, or shareholders, but contends that the primary source of income is not public or private charity. The Department also claims that the taxpayer does not benefit an indefinite number of people because the purpose of the organization is to support the development of housing and related commercial facilities. The Department claims that the taxpayer is not reducing any government burdens with its activities because the government is not burdened with providing any services that the taxpayer provides. Finally, the Department claims that the taxpayer does not provide charity to all who need and apply for it and places obstacles in the way of those seeking charity because the taxpayer's primary activity is not charitable. The primary activity involves the assembly of a team of entities or people aimed at developing area housing.

In response, the taxpayer states that it strongly disagrees with the Department's arguments because the taxpayer was created solely as a charitable organization. The taxpayer argues that its purpose is to redevelop abandoned property around the LOCAL Church and sponsor applications for funding sources. The taxpayer states that all the money it receives is either put back into the community or used to fund other charitable entities such as the DEF Center. The taxpayer also states that 2 years ago it received an abandoned factory that has 100,000 square feet, and the taxpayer intends to seek tax credits so that the building can be rehabilitated as a community center and as affordable housing units. The taxpayer states that in order for it to apply for tax credits, the taxpayer must be a not-for-profit. The taxpayer strongly believes that it is entitled to an exemption as a charitable organization.

In order to determine whether the taxpayer is a charitable organization for purposes of receiving an exemption identification number, the taxpayer's primary activity must first be determined. An exclusively charitable purpose is not interpreted literally to mean the organization's sole purpose; it is construed to mean the primary purpose but not an incidental or secondary purpose. Gas Research Institute, at 436. If a substantial purpose or activity of the taxpayer is not charitable, it cannot be said to be organized and operated exclusively for charitable purposes within the meaning of the Act. *Id.*

From the evidence presented, the taxpayer's primary activity is to organize the development of low-income housing and related commercial facilities. During the hearing, the taxpayer's executive director repeatedly described the taxpayer as a "community organizer." He explained that the taxpayer was organized as a not-for-profit so that it could apply for low-income housing tax credits, and then a for-profit entity,

such as COMMUNITY, acquires the credits from the taxpayer. (Tr. pp. 9-10) The end result is that the taxpayer gets developers to build the low-income housing, and the taxpayer receives the developer's fees.

Although the taxpayer's primary activities are commendable and significantly improve the quality of living in the area, they do not constitute a charitable activity for purposes of allowing an exemption identification number. In Provena Covenant Medical Center v. Department of Revenue, 384 Ill. App. 3d 734 (4th Dist. 2008), *aff'd*, 236 Ill. 2d 368 (2010), the court reaffirmed that charity is a "gift." See Provena, at 750. "'Charity' is an act of kindness or benevolence... 'Charity' is 'generosity and helpfulness, especially toward the needy or suffering'...." *Id.* The court added that to be charitable, an organization must give liberally. *Id.* The court also stated that a gift is, by definition, free goods or services. *Id.*, at 751.

The taxpayer's primary activity of organizing the development of affordable housing or other commercial facilities does not involve free goods or services. The taxpayer is compensated for its services with developer's fees. The taxpayer's primary activity is not, *per se*, a charitable activity because it does not involve a gift.⁴

Although the taxpayer is exempt from federal income taxes under section 501(c)(3) of the Internal Revenue Code as a charitable organization, in order to receive an exemption from retailers' occupation and use taxes, the taxpayer must meet the guidelines in Methodist Old Peoples Home, *supra*. The evidence does not show clearly and convincingly that the taxpayer meets most of the guidelines. The taxpayer meets part

⁴ The taxpayer's Organization Narrative refers to some activities that may be considered charitable (*e.g.*, community gardens and providing computers for local youth and families), but no additional information was given concerning these activities. From the evidence presented, these few potentially charitable activities are incidental and not the primary purpose of the organization.

of the second guideline because it does not have capital, capital stock, or shareholders. The taxpayer also meets the fourth guideline because without employees, there is no gain or profit in a private sense to any person connected with it. Nevertheless, the taxpayer's primary source of income is developer's fees and rent, not public or private charity, so it fails to meet the second part of the second guideline. The taxpayer also does not meet the first guideline because the taxpayer's activities directly benefit the developers and the for-profit LLCs that own the developed property. The general public is only an indirect beneficiary of the taxpayer's primary activity. Finally, as explained earlier, the taxpayer does not provide charity, so it does not meet the third, fifth, and sixth guidelines.

As previously mentioned, the taxpayer's primary activities are commendable, but laudable acts do not necessarily constitute charity. Rogers Park Post No. 108, American Legion v. Brenza, 8 Ill. 2d 286, 291 (1956); Turnverein Lincoln v. Board of Appeals of Cook County, 358 Ill. 135, 144-145 (1934). The taxpayer must establish clearly and convincingly that it is organized and operated primarily for charitable purposes. Exemption provisions are strictly construed, and all doubts must be resolved in favor of taxation. Rogy's New Generation, *supra*; Wyndemere, *supra*; Gas Research Institute, *supra*. Because the evidence presented falls short of showing clearly and convincingly that the taxpayer has met its burden of proof, the exemption must be denied.

Recommendation:

For the foregoing reasons, it is recommended that the taxpayer's request for an exemption identification number be denied.

Enter: July 25, 2019

Linda Olivero
Administrative Law Judge